

Service Date: August 4, 2006

DEPARTMENT OF PUBLIC SERVICE REGULATION  
BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MONTANA

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IN THE MATTER OF MONTANA-DAKOTA	)	UTILITY DIVISION
UTILITIES CO., Application for Annual Review )		
of Monthly Gas Cost Tracking Adjustment	)	DOCKET NO. D2003.4.49
Procedure and Final Approval of Interim Rates	)	
Resulting from that Procedure	)	ORDER NO. 6691b

IN THE MATTER OF MONTANA-DAKOTA	)	UTILITY DIVISION
UTILITIES CO., Application for Annual Review )		
of Monthly Gas Cost Tracking Adjustment	)	DOCKET NO. D2004.4.55
Procedure and Final Approval of Interim Rates	)	
Resulting from that Procedure	)	ORDER NO. 6691b

IN THE MATTER OF MONTANA-DAKOTA	)	UTILITY DIVISION
UTILITIES CO., Application for Annual Review )		
of Monthly Gas Cost Tracking Adjustment	)	DOCKET NO. D2004.5.69
Procedure and Final Approval of Interim Rates	)	
Resulting from that Procedure	)	ORDER NO. 6691b

**FINAL ORDER**

**Introduction**

1. Montana-Dakota Utilities Co. (MDU) implements monthly natural gas rate adjustments through a monthly gas cost tracking procedure approved by the Public Service Commission (PSC). MDU's monthly adjustments are interim (temporary) adjustments, pending annual review by the PSC. The above consolidated dockets are MDU's annual applications for PSC review and final approval of the interim rates resulting from MDU's monthly gas cost tracking adjustments for the tracking periods June 2002 through May 2003 (PSC Docket No. D2003.4.49), June 2003 through May 2004 (PSC Docket No. D2004.4.55), and June 2004 through May 2005 (PSC Docket No. D2004.5.69).

2. The Montana Consumer Counsel (MCC) has intervened in these consolidated MDU dockets and is the only person to do so. MCC and PSC audits and discovery have demonstrated no specific problems regarding MDU's monthly tracker adjustments or MDU's ongoing compliance with the monthly gas cost tracking procedure. Public hearing on these dockets was held on May 10, 2006, in Billings, Montana. The

only issue contested between MCC and MDU at hearing on this matter is whether MDU should be required to consider implementation of a financial hedging program for the purpose of ensuring price stability. MCC requests that the PSC direct MDU to consider such programs. MDU has provided information regarding the costs and potential problems involved with financial hedging programs and has suggested that individual customers interested in price stability might achieve a similar result through MDU's budget billing program.

#### Findings of Fact and Discussion

3. All introductory statements that can properly be considered findings of fact and that should be considered as such to preserve the integrity of this order are incorporated herein as findings of fact.

4. MDU's monthly gas cost tracking procedure, including the annual true-up component of that procedure, was approved by the PSC in 1997. *See PSC Docket No. D97.3.43, Order No. 5994, August 1, 1997.* MDU has since implemented the gas cost tracking procedure, increasing or decreasing gas prices on a monthly basis, so long as the monthly adjustment has met the threshold change of at least \$0.10 per dekatherm. MDU's monthly tracker adjustments for the periods involved in these consolidated dockets are summarized as follows:

DOCKET NO. D2003.4.49, ORDER NO. 6691b  
DOCKET NO. D2004.4.55, ORDER NO. 6691b  
DOCKET NO. D2004.5.69, ORDER NO. 6691b

3

a. June 2002 through May 2003 (PSC Docket No. D2003.4.49)

	RESIDENTIAL AND GENERAL SERVICE \$ PER DKT		LARGE INTERRUPTIBLE \$ PER DKT	
MONTH	COST OF GAS	CHANGE	COST OF GAS	CHANGE
JUNE 2002	\$3.278	(0.547)	\$2.328	(0.530)
JULY	\$2.736	(0.542)	\$1.796	(0.532)
AUGUST	\$2.397	(0.339)	\$1.451	(0.345)
SEPTEMBER	\$2.766	0.369	\$1.819	0.368
OCTOBER	\$2.313	(0.453)	\$1.364	(0.455)
NOVEMBER	\$2.310	(0.003)	\$1.812	0.448
DECEMBER	\$3.624	1.314	\$3.022	1.210
JANUARY 2003	\$4.571	0.947	\$3.971	0.949
FEBRUARY	\$4.262	(0.309)	\$3.653	(0.318)
MARCH	\$4.910	0.648	\$3.771	0.118
APRIL	\$6.664	1.754	\$5.652	1.881
MAY	\$5.097	(1.567)	\$4.209	(1.443)
TOTAL		1.272		1.351

b. June 2003 through May 2004 (PSC Docket No. D2004.4.55)

	RESIDENTIAL AND GENERAL SERVICE \$ PER DKT		LARGE INTERRUPTIBLE \$ PER DKT	
MONTH	COST OF GAS	CHANGE	COST OF GAS	CHANGE
JUNE 2003	\$5.560	0.463	\$4.664	0.455
JULY	\$6.598	1.038	\$5.709	1.045
AUGUST	\$6.309	(0.289)	\$5.427	(0.282)
SEPTEMBER	\$5.650	(0.659)	\$4.774	(0.653)
OCTOBER	\$6.020	0.370	\$5.143	0.369
NOVEMBER	\$5.825	(0.195)	\$4.806	(0.337)
DECEMBER	\$5.825	0.000	\$4.806	0.000
JANUARY 2004	\$6.211	0.386	\$5.187	0.381
FEBRUARY	\$6.642	0.431	\$5.634	0.447
MARCH	\$6.642	0.000	\$5.634	0.000
APRIL	\$6.221	(0.421)	\$5.344	(0.290)
MAY	\$6.315	0.094	\$6.640	1.296
TOTAL		1.218		2.431

c. June 2004 through May 2005 (PSC Docket No. D2004.5.69)

	RESIDENTIAL AND GENERAL SERVICE \$ PER DKT		LARGE INTERRUPTIBLE \$ PER DKT	
MONTH	COST OF GAS	CHANGE	COST OF GAS	CHANGE
JUNE 2004	\$6.970	0.655	\$7.297	0.657
JULY	\$7.758	0.788	\$8.077	0.780
AUGUST	\$7.399	(0.359)	\$7.712	(0.365)
SEPTEMBER	\$7.399	0.000	\$7.712	0.000
OCTOBER	\$6.548	(0.851)	\$6.860	(0.852)
NOVEMBER	\$6.548	0.000	\$6.860	0.000
DECEMBER	\$8.408	1.860	\$8.542	1.682
JANUARY 2005	\$7.813	(0.595)	\$7.938	(0.604)
FEBRUARY	\$7.813	0.000	\$7.938	0.000
MARCH	\$7.813	0.000	\$7.938	0.000
APRIL	\$7.607	(0.206)	\$7.762	(0.176)
MAY	\$8.419	0.812	\$7.925	0.163
TOTAL		2.104		1.285

5. MDU states that the monthly gas cost tracking procedure continues to achieve its objectives, including making gas costs reflective of the market in a timely manner, promoting customer understanding by pricing closer to actual price-affecting events, providing proper and timely price signals to customers, and minimizing the unreflected gas cost account balance to avoid cost shifts from one period to another.

6. MDU states that it purchases most of its natural gas supplies directly from producers through mid- to long-term contracts in which price is tied to a market-price index. MDU explains that the nature of its natural gas system justifies this approach to gas supply acquisition. In support of this procurement strategy MDU explains that:

- a. MDU's approximately 20 suppliers (at any given time) are producers located in MDU's four state operating region and Canada and are on or near the same pipeline system through which MDU obtains and distributes supplies;
- b. MDU's system constraints require a diversified set of suppliers, lengths of contracts, and contract end dates to ensure reliability;

c. MDU's suppliers have traditionally indicated little or no interest in selling natural gas through fixed-price, long-term contracts;

d. MDU's suppliers will not sell natural gas through long-term, fixed-price contracts because producer payments to production-related working interests, royalty holders, and taxing jurisdictions are based on market-price and there is a significant risk of supplier liability if the long-term fixed price were to be less than the market price;

e. natural gas marketers, as opposed to natural gas producers, have a limited presence on MDU's natural gas system and those marketers that have a presence are competing with MDU for purchases from MDU's suppliers; and

f. markets and marketers that might be willing to provide long-term, fixed-price contracts are located several pipelines away from MDU and transportation costs and transportation capacity limitations would become significant supply-cost factors.

7. The PSC finds that MDU's procurement practices are acceptable given the circumstances that exist regarding MDU's natural gas system at the present time.

8. The PSC's experience with the use of financial hedging (*e.g.*, financial derivatives) includes a 1995 application by MDU for a Gas Commodity Hedging Policy. *PSC Docket No. 95.1.2*. During that case PSC staff and MCC raised a number of concerns about financial hedging both in data requests and in meetings with MDU. On June 29, 1995, MDU filed a motion to dismiss its hedging application. That motion was granted and the filing was dismissed. MDU pursued financial hedging with the blessing of North Dakota, South Dakota, and Wyoming. Ultimately, MDU lost millions of dollars in its hedging program. Those losses were charged to ratepayers in the other three states. Ratepayers in Montana were not affected because the use of financial derivatives was not approved in Montana.

9. In recent years MCC has been urging the use of financial derivatives. There has been no evidence presented by MCC that demonstrates that there would be a clear benefit from the use of financial hedging. Given the PSC's experience with MDU, the PSC is concerned about making the decision to proceed with financial hedging. MCC has not provided any information for the PSC to consider with respect to the cost of financial hedging. Another reason that the PSC is concerned is the cost of financial hedging. Over the long run a hedged portfolio will be more expensive than a portfolio without hedging due to the transaction

costs associated with the hedges. Given that hedging costs would mount steadily through time, the cost issue is very important. There have been numerous examples in past years of hedging programs that lost substantial amounts of money. Given the concerns with respect to cost, the complexity and risk associated with financial hedging, the questionable benefit to consumers, and the experience with MDU's previous hedging program, the PSC declines to require MDU to consider the use of financial hedging programs. The PSC has recently made a similar decision regarding NorthWestern Energy's natural gas procurement practices. *See, Matter of NorthWestern Energy, PSC Docket No. D2006.2.21, PSC Comments, June 23, 2006 (corrected service date).*

#### Conclusions of Law and Discussion

10. All findings of fact that can properly be considered conclusions of law and that should be considered as such to preserve the integrity of this order are incorporated herein as conclusions of law.

11. MDU is a public utility within the meaning of that term at § 69-3-101, MCA. The PSC has jurisdiction over MDU in regard to this matter pursuant to Title 69, MCA. MDU's gas cost trackers for the rate-effective months of June 2002 through May 2005 have been filed and processed in accordance with the law and applicable MDU tariffs.

12. MDU's applications have been properly noticed and heard in accordance with Title 69, Chapter 12, MCA, and Title 2, Chapter 4, MCA (Montana Administrative Procedures Act).

13. The rates resulting from MDU's monthly gas cost tracking procedure for the periods affected by this order are just and reasonable and are hereby approved on a final basis.

14. MDU's monthly gas cost tracker procedure is approved for an additional year, to expire at the time the PSC issues an order following review of MDU's next annual gas cost true-up procedure, unless MDU demonstrates at that time sufficient cause to continue the monthly gas cost tracker.

15. The PSC determines that there is no compelling reason to require MDU to consider implementation of a financial hedging program.

DOCKET NO. D2003.4.49, ORDER NO. 6691b  
DOCKET NO. D2004.4.55, ORDER NO. 6691b  
DOCKET NO. D2004.5.69, ORDER NO. 6691b

7

ORDER

16. All conclusions of law that can properly be considered an order and that should be considered as such to preserve the integrity of this order are incorporated herein as an order.

17. All pending objections, motions, and arguments not specifically having been ruled on in this order (if any) shall be deemed denied, to the extent that such denial is consistent with this order.

18. The PSC, being fully apprised of all premises, hereby orders that MDU's monthly rate changes for the periods represented in MDU's 2003, 2004, and 2005 applications for annual PSC review are approved on a final basis.

Done and dated this 1st day of August, 2006, by a vote of 5-0 overall and 4-1 on the issue of financial hedging (*e.g.*, ¶ 9).

DOCKET NO. D2003.4.49, ORDER NO. 6691b  
DOCKET NO. D2004.4.55, ORDER NO. 6691b  
DOCKET NO. D2004.5.69, ORDER NO. 6691b

8

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION

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GREG JERGESON, Chairman

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BRAD MOLNAR, Vice-Chairman

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DOUG MOOD, Commissioner

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ROBERT H. RANEY, Commissioner

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THOMAS J. SCHNEIDER, Commissioner  
(voting to dissent on the issue of financial hedging)

ATTEST:

Connie Jones  
Commission Secretary

(SEAL)

NOTE: Any interested party may request the Commission to reconsider this decision. A motion to reconsider must be filed within ten (10) days. See 38.2.4806, ARM.